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PORTFOLIO ADVISORY INSIGHTS

Why increased recession risk doesn't mean major portfolio changes

The recent banking crisis need not result in the collapse of several more banks. However, we think a good old fashioned credit crunch in the US and Europe is now quite likely. And that is more likely than not going to result in a recession.

Our outlook has materially changed

- Credit standards were already tight - and further tightening is likely.
- Credit spreads have already widened sharply, and could widen further.
- A credit crunch will probably result in a sudden end to labour hoarding and an increase in unemployment.
- The credit impulse is slowing and a fall below -2% is probable, coinciding with a recession.
- The recent developments make it even more likely the Fed pauses rate hikes after the March hike.
- The yield curve has started its normalisation - a sign that Fed policy is too restrictive.

However, our portfolio positioning has not had to materially shift.

- We have been adding exposure to government bonds since last year as yields soared.
- More recently, we have been adding exposure to shorter-dated US treasuries.
- This was funded out of equities - not because they were bad value - but to be aware of downside risks.

These portfolio actions continue to make sense. While markets remain extremely volatile in the near-term, we expect preparing portfolios for downside risk now will pay off later.

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